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Investment Management Regulatory Update - June 2022

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In this issue, we discuss, among other things, proposed amendments to the "Names Rule" under the Investment Company Act, and proposed disclosure requirements for investment advisers and registered funds regarding ESG investment practices.

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SEC proposes amendments to the Investment Company Act "Names Rule" to prevent misleading or deceptive fund names
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Rules and regulations

SEC proposes amendments to the Investment Company Act "Names Rule" to prevent misleading or deceptive fund names

Summary

In a May 25, 2022 release (Proposing Release), the Securities and Exchange Commission (SEC) proposed amendments (Proposal) to the Names Rule (as defined below) under the Investment Company Act of 1940, as amended (Investment Company Act). The Proposal is designed to ensure that the name of a registered investment company or business development company (fund) accurately reflects the fund's investments and risks. Some key takeaways of the Proposal include:

– Broadened scope of the Names Rule's 80% investment policy requirement.

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- Prescribed circumstances under which a fund may "drift" below its 80% investment policy and a requirement to come back into compliance as soon as reasonably practicable, in most cases, within 30 days.
- Enhanced prospectus disclosure requirements regarding the definition of terms used in a fund's name, including with respect to the specific criteria used to select investments described by such terms.
- Additional reporting and recordkeeping requirements regarding a fund's compliance with its 80% investment policy.
- Specific provisions to address the use of environmental, social and governance (ESG) terms in fund names, and the treatment of derivatives in calculating a fund's compliance with its 80% investment policy.

Background

According to the Proposing Release, the SEC recognizes that a fund's name serves as an important marketing tool and can have significant impact on an investor's investment decisions. In 2001, the SEC adopted Rule 35d-1 under the Investment Company Act (Names Rule), which requires a fund with a name that suggests its focus is on a particular geographic region, industry, or type of investment must adopt a policy to invest at least 80% of its assets in a manner consistent with such suggested focus. The Proposing Release noted that the fund industry has seen significant growth and change over the last 20 years, including a rise in funds with thematic focus, such as a focus on ESG factors, an increase in the total assets under management, and an increase in fund types and strategies. As the fund industry has evolved, the SEC has observed interpretive issues in the application of the Names Rule which may have investor protection implications. For example, according to the Proposing Release, the SEC has previously taken the position that fund names which include terms such as "growth" and "value" that indicate a particular investment objective, strategy or policy, do not implicate the 80% investment policy requirement, even though such name can also indicate a particular investment focus to investors. In the Proposing Release, the SEC recognized that this issue can be particularly salient when evaluating the practices of funds with names that use ESG terminology. The SEC is therefore proposing amendments to the Names Rule in order to address these interpretive challenges, and to modernize and enhance investor protections.

Proposed amendments

Expansion of scope

The Proposal would broaden the scope of the current 80% investment policy requirement of the Names Rule to also apply to any fund whose name suggests that the fund focuses on investments that have, or whose issuers have, specific characteristics. The Proposal specifically calls out as examples of fund names that would be subject to the rule those names that include terms such as "growth," "value" or terms that indicate that the fund's investment strategy or decisions incorporate one or more ESG factors.

Plain English requirements for terms used in fund names

Under the Proposal, the terms used in the name of a fund that is required to adopt the 80% investment policy must be consistent with those terms' plain English meaning. The SEC's view is that terms used in a fund's name cannot be altered by disclosure and that defining such terms in a way that is inconsistent with their plain English meanings would be viewed as materially misleading.

Materially deceptive and misleading use of ESG terminology

To address "greenwashing" concerns, the Proposal specifically provides that the use of ESG terminology in a fund's name is "materially deceptive and misleading" if the fund is what the SEC views as an integration fund, i.e., a fund that considers ESG factors alongside other, non-ESG factors in its investment decisions, where such ESG factors are "generally no more significant than other factors in the investment selection process, such that ESG factors may not be determinative in deciding to include or exclude any particular investment in the portfolio."

Changes over time and temporary departures from a fund's 80% investment policy

The Proposal would amend the current Names Rule requirement that a fund must comply with its 80% investment policy "under normal circumstances," which currently provides funds with some flexibility to determine what would be considered outside of "normal circumstances." Instead, the Proposal would prescribe the specific circumstances under which a fund may depart from its 80 percent investment policy, i.e.:

1. As a result of market fluctuations or other circumstances not caused by the purchase or sale of a security or the entering or exiting of an investment by the fund;

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2. To address unusually large cash flows or redemptions;
3. To take positions in cash and cash equivalents or government securities to avoid losses in adverse market, economic, political or other conditions; or
4. To reposition or liquidate assets in connection with a reorganization, to launch the fund, or when a notice of change in the fund's 80% investment policy has been provided to the investors no less than 60 days before such change.

Under the Proposal, funds are required to return to compliance with its 80% investment policy as soon as reasonably practicable and cannot be out of compliance for more than 30 consecutive days, except in the case of a fund launch (in which case departures must not exceed 180 consecutive days), reorganizations (for which the Proposal does not specify a required time period), or when the 60 days prior notice is provided to shareholders for a change in such policy.

Derivatives

To reduce the risk of a fund using derivatives in a manner that is not consistent with the investment focus suggested by the fund's name, the Proposal addresses the valuation of derivatives, and the types of derivatives to be included in the 80% basket, for purposes of calculating a fund's compliance with its 80% investment policy. According to the Proposing Release, the notional value of a derivative is generally a better reflection of its investment exposure than its market value, and therefore, the Proposal would require a fund to calculate its 80% investment requirement using the notional values of derivatives. In addition, to avoid double-counting a fund's exposure through such derivatives for purposes of the 80% investment policy calculation, the Proposal would require a fund to reduce the value of its assets by excluding cash and cash equivalents up to the notional amount of the fund's derivatives, because such cash and cash equivalents generally serve as collateral for derivative instruments whose notional value would already be captured. The Proposal would also allow a fund to include in its 80% basket a derivatives instrument that provides exposure to one or more of the market risk factors (e.g., currencies) associated with the investments suggested by the fund's name, in addition to derivatives that provide exposure to the particular investments suggested by the fund's name.

Unlisted closed-end funds and BDCs

Given the limited exit options for shareholders of registered closed-end funds and BDCs whose shares are not listed on a national exchange, the Proposal would require the 80% investment policy for such funds to be a fundamental policy, which cannot be changed without shareholder approval.

Enhanced prospectus disclosure

The Proposal would amend Form N-1A, Form N-2, Form N-8B-2, and Form S-6 to require each fund that is subject to the 80% investment policy requirement to include disclosure in its prospectus that defines the terms used in the fund's name, including the criteria used to select the investments described by such terms. In addition, funds would be required to tag new information using a structured data language (i.e., Inline XBRL).

N-PORT reports

Under the Proposal, registered investment companies (other than money market funds and BDCs) that are required to adopt an 80% investment policy would be required to report on Form N-PORT:

– The value of the fund's 80% basket, as a percentage of the value of the fund's assets;
– The number of days that the fund fell below its 80% investment policy during the applicable reporting period; and
– With respect to each portfolio investment, whether such investment is included in the fund's 80% basket.

The SEC believes these amendments will allow it to better assess an individual fund's compliance with the Names Rule, as amended, as well as conduct market-wide assessments.

Reporting and recordkeeping

The Proposal would impose new recordkeeping requirements on funds that are subject to the 80% investment policy requirement. The Proposal would require such funds to maintain written records to document their compliance with the 80% investment policy, including:

– The fund's record of which investments are included in the fund's 80% basket and the basis for including each such investment in the 80% basket;
– The value of the fund's 80% basket, as a percentage of the total value of the fund's assets;
– The date of any departures from the 80% investment policy and the reason for such departures; and

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– Any notice sent to the fund's shareholders pursuant to the amended Names Rule.

These records would be required to be maintained for at least six years following the creation of such records. For a fund that does not adopt an 80% investment policy, the Proposal would require a written record of the fund's determination that it is not subject to the 80% investment policy requirement under the amended Names Rule.

Unit investment trusts

The Proposal would exempt unit investment trusts (UITs) that made their initial deposit of securities before the effective date of the final amendments from the 80% investment policy requirement and related recordkeeping requirements. Under the SEC's view, this approach is generally consistent with the treatment of UITs under the current rule.

Transition period

The SEC proposed a one-year transition period from the date of publication of the final rule in the Federal Register, if adopted, to provide time for funds to prepare for compliance with the final rule.

The SEC has requested public comments on the Proposal, to be received by the SEC on or before August 16, 2022.

SEC proposes enhanced disclosure requirements for investment advisers and registered investment companies regarding ESG investment practices

Summary

In a May 25, 2022 release (Proposing Release), the SEC proposed amendments (Proposal) to rules and forms under the Investment Advisers Act of 1940, as amended (Advisers Act), and the Investment Company Act, with respect to disclosure of ESG investment practices in fund registration statements, fund annual reports, adviser brochures and census-type reports, including: Forms N-1A, N-2, N-CSR, N-8B-2, S?6, N-CEN and Form ADV. The Proposing Release notes that the Proposal is designed to facilitate enhanced disclosure of ESG practices to clients and shareholders in order to create a consistent disclosure framework, as "[i]t is important that investors have consistent and comparable disclosures about asset managers' ESG strategies so they can understand what data underlies funds' claims and choose the right investments for them." The Proposal would apply to registered and certain exempt investment advisers (advisers), registered investment companies and business development companies (funds).

The SEC was prompted to issue the Proposal by the inconsistency of information provided by funds and advisers to investors regarding the ESG factors that such funds and advisers use in their investment strategies. According to the Proposing Release, there is currently no standard for how funds and advisers report ESG factors, and therefore it is difficult for investors to determine what ESG strategies the funds and advisers employ, whether the funds and advisers are meeting the ESG-related targets they claim to meet and whether the strategies funds and advisers employ are effective. In response, the Proposal is designed to create consistent standards for funds and advisers to disclose ESG-related strategies. These disclosures would apply to disclosures to investors and in regulatory reporting regarding ESG-related strategies. The Proposal also includes amendments to Form N-CEN that would require index funds to report certain information about the index, regardless of whether the fund tracks an ESG-related index. The Proposal also will require funds to submit these ESG-related disclosures in a structured data language so the data can be readily analyzed.

The SEC has requested public comments on the Proposal, to be received by the SEC on or before August 16, 2022.

Some key takeaways of the Proposal include:

– Categorization of funds based on how they integrate ESG factors and strategies, and enhanced ESG disclosure requirements based on such categorizations:
  - ESG-Focused Fund: A fund that focuses on one or more ESG factors and uses such factors as a significant or main consideration in selecting investments or in its engagement strategy with companies in which it invests. According to the Proposing Release, such factors could include, among others, screens for carbon emissions, board or workforce diversity and inclusion, or industry-specific issues. This category specifically includes funds with a name that indicates that the fund's investment decisions incorporate one or more ESG factors, and funds whose advertisements and marketing materials indicate that the fund's investment decisions incorporate one or more ESG

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factors as a significant or main consideration in selecting investments.

  - Impact Fund: An ESG-Focused Fund that seeks to achieve specific ESG impacts or generate specific ESG-related benefits.
  - Integration Fund: A fund that considers one or more ESG factors alongside non-ESG factors in investment decisions, where such ESG factors are generally not more significant than other factors in the investment selection process (i.e., ESG factors may not be determinative in decisions to include or exclude particular investments).

- Requirements for funds to tag ESG disclosures using a structured data language known as the Inline eXtensible Business Reporting Language (Inline XBRL).
- Requirements for Impact Funds to disclose progress in achieving stated impacts and factors affecting the fund's ability to achieve such impacts.
- Requirements for funds that use proxy voting as a significant means of implementing its ESG strategy to disclose information on how it voted its proxies on ESG-related voting matters and information regarding ESG engagement meetings.
- Requirements for funds that consider environmental factors in their investment decisions and strategy to disclose information and metrics regarding their evaluation of greenhouse gas emissions (GHG).

Background

As discussed in the Proposing Release, in the 1970s and 1980s, asset managers began to integrate ESG factors into funds with social and environmental investment objectives, and the first socially responsible index was launched in the 1990s. Beginning in the mid-2000s, many financial institutions signed on to climate and sustainability-related investment frameworks and a variety of organizations were formed to create disclosure frameworks designed to consider environmental measures. As a result, the asset management industry has increasingly focused on environmental issues related to climate change, among other issues and an "increasing number of funds market themselves as 'green,' 'sustainable,' 'low-carbon,' and so on." According to the Proposing Release, there has been a rapid increase in investors seeking to invest in ESG-related strategies, funds and services. Funds and advisers are subject to general disclosure requirements concerning investment strategies and are required to disclose certain information, such as material information on investment strategies, risks, governance and fund performance. However, while ESG-related strategies may fall into these categories of required disclosures, the Proposing Release noted that there are no specific requirements regarding the information funds and advisers must disclose about their ESG-related investment strategies and, as a result, there is "currently a huge range of what asset managers might disclose or mean by their claims." Because there is currently no specific disclosure framework, there is a risk of funds and advisers marketing themselves as focusing on ESG factors when in actuality their ESG strategies are limited, which is misleading to investors. Additionally, because inconsistent information is provided about funds' and advisers' ESG-related investment strategies, it is difficult for investors to understand such strategies and to compare strategies across various funds and advisers. In response, the SEC has submitted the Proposal, which is designed to create a consistent disclosure regime that standardizes ESG reporting and requires funds and advisers to disclose specific and detailed information about their ESG-related investment strategies. The Proposal is intended to enhance disclosure so that investors and the public have more information about funds' and advisers' ESG investment strategies and are better able to understand and compare ESG investment strategies. Further, requiring specific and standardized reporting seeks to prevent funds and advisers from making exaggerated claims about their ESG investment strategies, thus protecting investors from potentially misleading claims.

Proposed amendments

Proposed prospectus ESG disclosures

The amount of additional disclosure that would be required for funds under the Proposal would depend on the extent to which the fund considers ESG factors in its investment strategies and decisions. Such ESG disclosures would be in addition to the information funds currently are required to disclose in the prospectus regarding their investments. Integration Funds would be required to provide relatively limited disclosure of their ESG investing strategies, while ESG-Focused Funds would be required to disclose more detailed information. These prospectus-related amendments would apply to both open-end and closed-end funds that consider one or more ESG factors in their investment process.

- Integration Funds

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    - Integration Funds would be required to briefly summarize how the fund incorporates ESG factors into the investment decision process, including the specific ESG factors the fund considers.
        - The SEC proposes a “layered disclosure” approach for disclosure of ESG information in the fund’s prospectus. Under this approach, key information about a fund’s ESG strategies would be included in the summary section of the prospectus for open-end funds, or in the general description of the fund for closed-end funds, while more detailed information about the fund’s investment strategy and use of ESG factors would be included in the statutory prospectus for open funds, or later in the prospectus for closed-end funds.
        - For Integration Funds that consider GHG emissions in its investment selection process, the fund would be required to describe how the fund considers GHG emissions of portfolio companies, including the fund’s methodology, which is intended to help investors better understand how a particular fund uses such data in making investment decisions.

- ESG-focused Funds and Impact Funds
    - ESG-Focused Funds and ESG Impact Funds would be required to provide specific disclosure on how the fund incorporates ESG factors in its investment process. Impact Funds would also be subject to additional requirements in order to clarify the specific impact the fund seeks to achieve and to discuss the progress the fund has made in achieving such impact.
    - These funds would be required to disclose their ESG strategies in an ESG Strategy Overview table in the fund’s prospectus. Open-end funds would include this information at the beginning of the “risk/return” summary. Closed-end funds would be required to provide this information at the beginning of the discussion of the fund’s organization and operation. In the ESG Strategy Overview table, a fund would be required to provide: (i) an overview of the fund’s ESG strategy, (ii) how the fund incorporates ESG factors in its investment decisions, and (iii) how the fund votes proxies and/or engages with companies on ESG issues. Requiring funds to disclose this information in the ESG Strategy Overview table is intended to streamline the disclosure so that it is easier for investors to find and compare relevant information across different ESG-Focused Funds and Impact Funds.
    - Also utilizing the layered disclosure approach, these funds would be required to provide brief descriptions in the ESG Strategy Overview table and more detailed disclosures in other sections of the prospectus.
    - Additional disclosures for Impact Funds
        - Impact Funds would also be required to disclose in the ESG Strategy Overview table a description of the impacts it seeks to achieve and how it seeks to achieve those impacts. This description must include how the fund measures progress in achieving its stated impact, including key performance indicators, the time horizon the fund uses to measure its progress, and the relationship between the stated impact and financial returns. Again, the table would include a brief overview of these points, which would be described in greater detail later in the prospectus.
        - Impact Funds would also be required to disclose in their investment objectives the ESG impact that they seek to achieve through their investments. For open-end funds, this would be disclosed at the beginning of the prospectus, and for closed-end funds, this would be disclosed where the fund first describes its investment objectives.

- UITs
    - Any UIT with portfolio securities chosen based on ESG factors would be required to explain how such ESG factors were used in the investment selection process.
    - Given the unmanaged nature of UITs, and “mirror voting” by UIT trustees, UITs would not be categorized as ESG-Focused Funds, Impact Funds, or Integration Funds and would not be required to disclose engagement with portfolio companies.

Proposed fund annual report ESG disclosure

The Proposal also would require additional ESG disclosure in the management’s discussion of fund performance (MDFP) or equivalent section of a fund’s annual report.

- Impact Funds would be required to discuss the fund’s progress in achieving the stated impact during the reporting period in qualitative and quantitative terms and to discuss the key factors materially affecting the fund’s ability to achieve such impact.

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- ESG-Focused Funds utilizing proxy voting as a significant means of implementing ESG strategies would be required to disclose information on how the fund voted proxies on ESG matters, which may be limited to ESG matters that the fund incorporates into its investment decisions. For example, the Proposal would require the fund to disclose the percentage of such ESG matters during the reporting period where the fund voted in favor of the particular ESG initiative. The fund (other than a BDC) would also be required to refer investors to its most recent full voting record reported on the fund's Form N-PX by cross-reference or hyperlink.
- Funds utilizing engagement with issuers as a significant means of implementing their ESG strategies would be required to discuss their progress "on any key performance indicators" and disclose the number or percentage of issuers with which the fund held ESG engagement meetings, as well as the total number of such meetings.
- ESG-Focused Funds that consider environmental factors as part of their strategy would be required to disclose the carbon footprint and the weighted average carbon intensity (WACI) of the fund's portfolio in the MDFP or equivalent section of the fund's annual report. Specifically, this requirement would be applicable to funds indicating that they consider environmental factors in response to Item C.3(j)(ii) on Form N-CEN (other than funds that state that they do not consider GHG emissions as part of their investment strategy in the ESG Strategy Overview table in the prospectus). The Proposal specifies how a fund should calculate the carbon footprint and WACI for its portfolio investments, including investments in operating companies and registered and private funds (other than money market funds). A fund would also be required to provide additional information on Form N-CSR regarding any assumptions and methodologies used in calculating its portfolio's GHG emissions, any limitations associated with such assumptions and methodologies, and explanations of any good faith estimates of GHG emissions the fund was required to make.

XBRL tagging proposals

The Proposal would require funds to submit all ESG-related disclosures filed with the SEC in Inline XBRL, which would allow investors, other market participants, and the SEC to easily extract and analyze the disclosed information. According to the Proposing Release, the requirements would allow for automated extraction and analysis of the disclosed data which would make it easier for users to analyze and compare data across funds.

Amendments to Form ADV Part 2A

The Proposal would also amend Form ADV Part 2A to include information about advisers' ESG practices. Such requirements would provide current and prospective investors with information to assist them in evaluating the ESG strategies and services the advisers utilize.

- The Proposal would add a new Item 8.D, which would require an adviser to describe the ESG factors it considers for each significant investment strategy in which it considers ESG factors and how the adviser incorporates these factors in providing investment advice. For any ESG impact strategy, the adviser would be required to describe how it seeks to achieve such impacts, including progress measurement, key performance indicators, time horizons and the relationship between such impact and financial returns.
- The Proposal would amend Item 10.C to require advisers to describe any relationship, material to the adviser's business or clients, that the adviser may have with related persons who are ESG consultants or ESG service providers. This disclosure is intended to help the SEC and clients determine whether such relationships create material conflicts of interests.
- The Proposal would amend Item 17.A to require advisers with specific voting policies that consider one or more ESG factors when voting client securities to disclose which factors they consider and how they consider them. Such disclosure is intended to provide investors with a better understanding of how the adviser engages with portfolio companies on ESG issues.
- Advisers that sponsor wrap fee programs and deliver a wrap fee brochure to their clients would be required to describe the ESG factors they consider and how they incorporate such factors into their wrap fee programs, including when selecting, reviewing or recommending portfolio managers for the program.

Reporting on Form N-CEN and ADV Part 1A

The Proposal would also amend Form N-CEN and ADV Part 1A to collect information on funds' and advisers' use of ESG factors. Such amendments seek to help the public and the SEC understand evolving trends relating to ESG investing.

- The Proposal would add an Item C.3(j) to Form N-CEN which would require funds to disclose information about their ESG strategies. If a fund indicates that it incorporates ESG factors into its investment decisions, it would be required to report the types of strategies it utilizes, the ESG factors it considers, and the method it uses to implement its ESG strategy.

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- The Proposal would amend Form ADV Part 1A to expand the information collected about the advisory services provided to separately managed account and private fund clients. Advisers would be required to disclose whether they consider ESG factors as part of significant strategies in the advisory services they provide to separately managed account or private fund clients, and whether they use an ESG-integration, ESG-focused approach and/or an ESG-impact approach. Advisers would also be required to disclose whether they follow any third-party ESG frameworks in connection with their advisory services.
- The Proposal would amend Items 6 and 7 of Form ADV Part 1A to require advisers to disclose whether they conduct other business activities as ESG providers or have related persons that are ESG providers, to allow investors to assess potential conflicts of interest and risks created by such relationships.

Compliance procedures and marketing

In the Proposing Release, the SEC emphasized the importance of reviewing the accuracy of statements regarding ESG investment strategies, and advisers' and funds' compliance obligations under relevant federal securities laws, including the Advisers Act and Investment Company Act. The SEC noted in particular the importance of reviewing statements regarding ESG strategies in marketing materials to ensure that such statements do not violate applicable rules, such as the Advisers Act marketing rule, regarding false and misleading advertisements.

Transition period

The SEC proposed a one-year transition period from the date of publication of the final rule in the Federal Register, if adopted, to provide time for advisers to prepare for compliance with the final rule.

Litigation

SEC settles with private equity firm over allegedly undisclosed allocation of fees and expenses

The SEC's 2022 Examination Priorities characterized "disclosure of fees and expenses" as a "perennial priority[]"—as reflected in a number of enforcement actions relating to fee and expense allocations over the past decade. Most recently, on June 14, 2022, the SEC issued an order (ECP Order) instituting and settling administrative and cease-and-desist proceedings against Energy Capital Partners (ECP), a private equity and credit investment adviser, arising out of allegedly undisclosed, disproportionate allocation of fees and expenses to certain investors in one of its managed private equity funds.

In 2013, ECP launched Energy Capital Partners III, LP (Fund III); that fund closed in April 2014 with approximately $5.05 billion in capital commitments. According to the ECP Order, Fund III's organizational documents disclosed that the fund would allocate fund expenses "based on the relative investment and/or benefits derived among" the funds, and/or "in any manner determined equitable, in the good faith judgment" of ECP.

In May 2017, Fund III entered into negotiations to acquire a certain target company; Fund III signed an agreement to purchase the target company in August 2017, under which Fund III was required to provide proof of funding for the approximately $5.5 billion equity component of the transaction. ECP directed that approximately $1.95 billion of Fund III's available capital be allocated to funding the transaction; the remainder would be funded by certain co-investors (which the ECP Order calls the "Pre-Deal Co-Investors") and a bridge facility.

In September 2017, ECP launched Energy Capital Partners IV, LP (Fund IV); ECP allegedly anticipated eliminating the bridge facility for the transaction by investing capital of Fund IV and certain co-investors (which the ECP Order calls the "Post-Deal Co-Investors"). Ultimately, when the transaction closed in March 2018, Fund III invested approximately $1.4 billion, the "Pre-Deal Co-Investors" invested approximately $2.55 billion, the "Post-Deal Co-Investors" invested approximately $1 billion, and Fund IV invested approximately $450 million.

As stated in the Order, although ECP intended to allocate approximately $27 million in fees for the bridge facility pro rata, the "Pre-Deal Co-Investors" objected to bearing any share of those fees. ECP allegedly agreed not to allocate any of the bridge facility fees to the "Pre-Deal Co-Investors," and, instead, allocated to Fund III approximately 39% of the bridge facility fees even though Fund III was allocated only 27% of the equity investment in the target. This decision allegedly caused Fund III to bear about $3.3 million more in expenses than it would have had the fees been allocated pro rata.

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The SEC asserts that ECP should not have allocated to Fund III more than its proportional share of the bridge fees absent disclosure in the organization documents or to Fund III investors by another means, thereby violating Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder. The SEC also alleges that ECP thereby failed to implement its written policies and procedures designed to prevent violation of the Advisers Act and rules relating to expense allocation, in violation of Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

The ECP Order notes that ECP remediated the allocation by paying to Fund III the excess $3.318 million (plus interest) in fees over what it would have had to bear had the fees been allocated pro rata.

ECP agreed to cease and desist from future violations, to be censured, and to pay a civil money penalty of $1 million.

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